Lecture 6. RELOCE 2010

Evidence and causes of economic disadvantage:
The case for regional policy

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Aims
- To discover the evidence of a "regional problem"
- Look at the causes from a number of perspectives
- Differentiate between economic development and economic regeneration
- Discover why regional policy is seen as a necessary part of government economic policy.
- Examine the two different theoretical/ideological approaches to reducing regional disparities.
- Review briefly the main phases of regional policy since 1928
- Examine the tension between social and economic objectives

Outcomes
- Be able to identify the difference in regional economic performance
- Have a working knowledge of some of the causes
- Be aware of the importance of regional economic policy
- Be conversant with the main differences in the theoretical approaches, how policy has evolved and the problems this throws up.

Evidence of a "Regional Problem"

The RELOCE course has already suggested that there is evidence of inequality of economic opportunity across the regions of the UK.

Previous Lectures

1. For instance, RELOCE lecture 9 examined regional migration and highlighted evidence of a North South divide in the UK.

2. Lecture 10 looked at unemployment disparities, this suggested that regional unemployment disparities in the UK had remained relatively intact since the slump of the 1930's, a period of almost 70 years.

Sharing the Nation's Prosperity

In December 1999 the Cabinet Office published a comprehensive paper entitled "Sharing the Nation's Prosperity – Variation in Economic & Social Conditions across the UK". Whilst the Report suggests that the health of regional economies is dependant on the UK macro economy enjoying long-term and stable growth, it concludes by listing new policy initiatives to combat inter and intra regional inequalities. The summary admits to regional disparities but suggests that these were less pronounced than in other EU countries. The main point the report was trying to make was that <u>the economic disparities within regions is at least as great as those between them</u>. *The report shows regional disparities in a variety of measures including:*

Disposable Income & Income Support
- Household sector income per head ranged from around £11,000 in London to just over £8,000 in the North East, in 1997.
- Households in the North East and London are twice as likely to be in receipt of Income Support as those in the South East.

Employment & Unemployment
- Between February and April 1999, 65.2 per cent of the population of working age in the North East were in employment, compared to the UK average of 73.9 per cent and 80.1 per cent of those in the South East were in employment, the highest proportion of any UK region.
- Unemployment in the South East, South West and East has remained consistently below the United Kingdom average since 1997. Unemployment in London has remained at a higher rate than its neighbouring regions, and in spring 1999 was one and a half percentage points above the national average of 6.3 per cent.

Business Survival

- Northern Ireland had the highest survival rate of business, after 12, 24 and 36 months, than anywhere else in the UK. The North West of England had the lowest survival rate after 12 months, while the West Midlands had the lowest survival rate after 24 months and the North East has the lowest survival rate after 36 months.

R & D

- Businesses in Wales spent the least on R&D as a proportion of GDP while those in the East spent the highest proportion - East spent more on R&D than the South East.

Educational attainment & Qualifications

- The percentage of UK pupils in their last year of compulsory education achieving 5 or more grades A* to C GCSE or SCE Standard Grades in 1996/97was highest in Scotland at 55 per cent, and lowest in the North East at 38 per cent.
- In Spring 1998 the South East and South West regions had the lowest proportions of the population of working age with no qualifications.

Housing

- The average house price in London in 1998 was around £130,000, more than double the price of houses in the North East, which had the lowest average house prices.

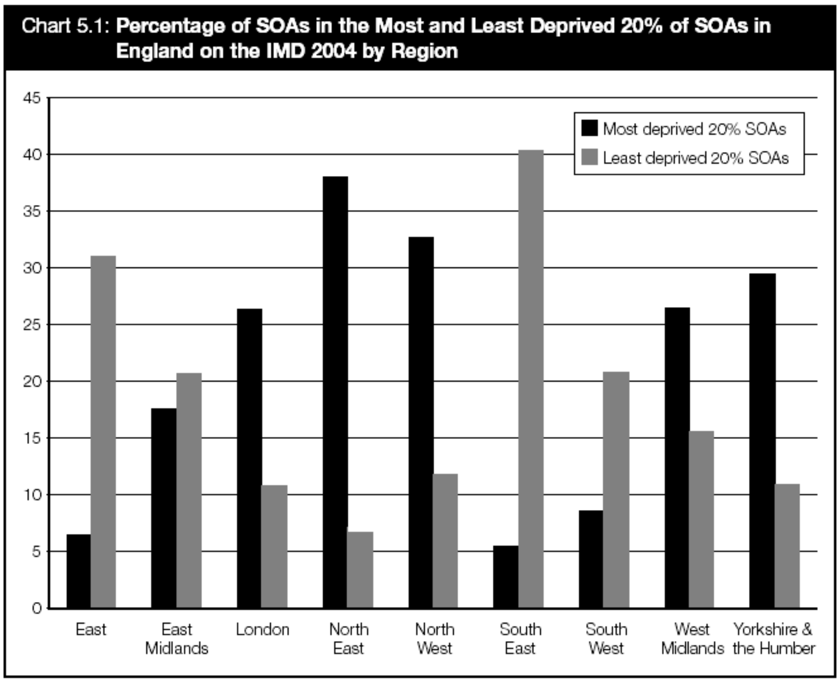
Crime

- The East of England had the lowest recorded crime rate in England and Wales in 1997, nearly 40 per cent lower than the rate in the Yorkshire and Humber region, which was the highest.

***ODPM Deprivation Index**.*

The cabinet office report uses the 1998 index of deprivation to highlight regional differences. The 2004 Deprivation index maps deprivation in greater detail by using Super Output Areas (SOA's).

- The most deprived 20% of areas are concentrated in cities, 'one-industry' towns and coalmining areas.
- Over 9.8 million people live in these areas representing 20% of the population of England.
- On average, just under a third of people in these areas are classified as income deprived.
- Over one in five (21.8%) of the relevant adult age group in these SOAs are employment deprived.
- Just under half (46.7%) of children in these areas live in families that are income deprived.
- Just under a third (30.1%) of older people in these areas are income deprived.



Source: The English Indices of Deprivation 2004, ODPM

Table 5.1: **Number of SOAs in the Most Deprived 20% of SOAs in England on the IMD 2004 by Region**			
	Number of SOAs in most deprived 20% of SOAs in England	**Number of SOAs in the region**	**% of SOAs in each region falling in most deprived 20% of SOAs in England**
East	220	3550	6.2
East Midlands	482	2732	17.6
London	1260	4765	26.4
North East	631	1656	38.1
North West	1461	4459	32.8
South East (excluding London)	271	5319	5.1
South West	278	3226	8.6
West Midlands	917	3482	26.3
Yorkshire & the Humber	976	3293	29.6
Total	**6496**	**32482**	**20**

Source: The English Indices of Deprivation 2004, ODPM

European disparities

There is also a wealth of evidence of regional disparities in the EU, for more details see the Third report on economic and social cohesion this is available from http://europa.eu.int/comm/regional_policy/sources/docoffic/official/reports/cohesion3/cohesion3_en.htm . Although the report suggests that there have been improvements in those countries receiving structural funds there is sluggish growth or divergence in disparities in others particularly southern Italy. For an earlier perspective which is decidedly less rosy see Convergence among regions of the European Union 1950 -1990, by Harvey Armstrong in Papers in Regional Science 1995.

International

Andrés Rodríguez-Pose and Nicholas Gill, in their paper Is there a global link between regional disparities and devolution?, Research Papers in Environmental and Spatial Analysis No. 79, Department of Geography & Environment, London School of Economics and Political Science, suggest that contrary to popular belief regional devolution has not led to decreases in regional disparities, in fact the opposite has occurred over the last 20 years. Using the variance of the natural logarithm of regional GDP per capita they show that disparities a increasing in both developed and developing countries.

Variance of the Log of regional GDP per capita						
	Year			**% Change**		
	1980	**1990**	**2000**	**1980-90**	**1990-00**	**1980-00**
Developing Countries						
China	0.578	0.483	0.581	-16.31	20.20	0.60
India	0.352	0.377	0.441	7.10	16.98	25.28
Mexico	0.388	0.383	0.435	-1.29	13.58	12.11
Brazil	0.588	0.488	0.494	-17.01	1.23	-15.99
Developed countries						
US	0.136	0.152	0.148	11.76	-2.63	8.82
Germany	0.184	0.188	0.186	2.17	-1.06	1.09
Italy	0.265	0.269	0.277	1.51	2.97	4.53
Spain	0.207	0.199	0.222	-3.86	11.56	7.25
France	0.151	0.164	0.163	8.67	-0.29	8.36
Greece	0.156	0.158	0.158	1.21	0.16	1.37
Portugal		0.231	0.236		1.85	
EU		0.247	0.275		11.24	

*Data for Europe: EU 1980-99; Greece 1981 – 1999; France 1982 – 1999. All others as shown.

Regional data from EUROSTAT and national statistical offices.

The causes of Economic Disadvantage- the economists perspective

Reference Harris (1991) Chapter 2

Harris examines the economy of Northern Ireland and highlights four outcomes of the region's poor economic performance. These include the chronic labour market imbalance (supply outstripping demand), and poor relative growth of manufacturing in the province in the immediate post war period:

High relative unemployment – unemployment was consistently higher in NI than the rest of the UK
High outward migration – migration was particularly high with the most able and dynamic leaving the province
Low earnings levels – significantly below the rest of the UK reducing regional demand
Low growth of capital stock (manufacturing) – A failure to invest in either existing sectors or diversify into new growth areas.

The reason is that Northern Ireland was chosen by Harris, was that it provides the most clear-cut example of a regional economy, which exhibits significant disparities compared with the UK average. He identifies 3 main reasons for poor manufacturing growth topic and two related issues that make the problem even more acute

- Structural – The local manufacturing stock was predominantly in sectors declining internationally and subject to intense overseas competition from emerging economies in the fare east and elsewhere. The main sectors were shipbuilding and textiles
- Location – NI is a peripheral region within both the UK and Europe. It is geographically distant from the centre of economic activity in the UK and Europe. As Europe turned inwards and UK became less dependant on the Empire for trade and raw materials so NI's previous strengths turned to weaknesses.
- Technology and productivity – The province had a low-technology industrial base, being reliant on cheap labour for its comparative advantage. This led to low levels of investment in capital stock and thus a lower productivity base than elsewhere in the UK. When even lower cost centres for labour opened up after the war NI found itself with both inefficient labour and worn out capital stock.

  - The linkages between local and regional economies and national demand – with NI the local economy was relatively small therefore local demand was not always sufficient for the establishment of efficient sectors within the province. Thus a high proportion of local demand was met by exports from elsewhere in the UK. This in turn gives an adverse regional balance of payments.
  - Adjustment to economic imbalance – there were not automatic stabilisers. Also there was little opportunity to trade out of the adverse conditions because of the state of capital stock and the deskilling of the labour force through migration.

Out-migration of labour and in-migration of capital occured in NI in the 1950's but not at a high enough level to compensate for the adverse terms of trade. Therefore, **Harris suggests that in the absence of automatic adjustment there was a strong case for implementing regional policies in Northern Ireland in the 1950's**

Economic Geographers perspective

Manners et al (1980) suggest that, the root cause of changes to economic geography lie in the evolution of consumer demands. The rise of the service sector is not conditional on the decline of manufacturing and resource based industries rather it is a function of changing consumer tastes as an increased proportion of wealth is spent on services such as health, education, travel, entertainment, recreation and personal services.

There has also been a change in locational preference for the country's industrial base – no longer is location reliant on one source of fuel. These locational shifts in turn throw up a number of related problems, competition for land, slow growth and stagnation, permanent environmental damage and the inability of inner city areas to adjust to change. **Sant (1974)**, suggests that "the basic cause of regional disparities is that countries lack an inherent mechanism to ensure that, in the long-term, the benefits of economic change are distributed equally on a per capita basis.

The problem of a lack of an automatic stabaliser identified by Harris was summed up by McCrone in 1969
"… it is therefore possible for a region to find that there is no product it can produce which other regions cannot peoduce more efficiently. Moreover, there is nothing to prevent a region from remaining in an adverse balance of payments relationship with the rest of the country for an indefinite period of time …. (this) has a depressing effect on the economy in the same way as an excess of savings over investment, and will tend through the multiplier to produce regional depression and unemployment."
McCrone, G (1969), Regional Policy in Britain Allen & Unwin, London, p80

Difference between Economic Development and Economic Regeneration

20 years ago economists - and policy makers would have been concerned about **economic development**. This is probably best described as national industrial policy enacted on a regional or local scale.
The objective was to **develop, or protect**, industrial sectors in a particular location via local, regional or national policies. Essentially the policies were aimed at helping firms (or the labourforce) via investment in companies. In particular policy sought to improve capital stock, subsidise employment to compensate for lower costs in other parts of the world, encourage companies to move to locations where unemployment was high and improve infrastructure in the vacinity of industrial complexes.

More recently the focus has switched to economic regeneration. The objective is to assist areas (and individuals) that are disdvantaged in some way, shape or form. Policy has become more and more concerned with the supply side in particular improving efficiency. Often a package of measures is put in place that are complementry such as, improved transport links, loan funding for initial site development, seedcorn money for R&D and subsidised staff training delivered through local colleges.

Why is regional policy a necessary part of government economic policy?

There is a strong case for regional policy on two grounds ***efficiency*** and ***equity.***

- ***Efficiency*** grounds relate to the best or optimal use of scarce resources i.e. not wasting the human and capital resources on unemployment and idle plant.
- ***Equity*** grounds suggest that continuing/high unemployment has harmful political and social consequences arising from deprivation.

Efficiency issues

A case can be made on efficiency grounds to justify deploying regional policy. Economic development is in its nature (spatially) uneven, and left to market mechanisms economic growth usually benefits the core rather than the periphery. There are a number of fairly obvious ***efficiency issues*** linked to bringing unused labour, capital and land back into use:

- Creating additional employment.
- Utilisation of underused land and capital
- More efficient use of social capital and public services.
- Reducing inflationary pressures by spreading capacity.
- Positive multiplier effects

Equity issues

Substantial differences in living standards cause dissatisfaction and resentment.

- Correlation between chronic unemployment and social factors – poor housing etc.,
- Thus it is argued that if unemployment can be reduced then social conditions will be improved and a net gain in social welfare will result.

See Armstrong and Taylor 2000 pp206 - 208

Theoretical approaches

Note that there is no disagreement that there is a “regional problem”. Differences emerge in **defining the root cause** and the **types of policy measures** that should be used to revive depressed regions. Armstrong and Taylor suggest that **markets are not particularly efficient** otherwise regional unemployment disparities would automatically be eliminated”. Minford and Stoney suggest that it is not the market that is at fault but that they **are prevented from operating efficiently by vested interests.**

Markets should clear But market forces appear to fail - why is this so?
Barriers to capital and labour migration:
Firms have a preference for current certainty; - Small firms loose local input / output linkages; There are also significant barriers to labour migration.
Wages fail to respond to local market conditions because of:
Collective agreements; Minimum wage; Unemployment benefit; Easy access to benefits; Poor policing of benefits.
There are two opposing policy responses to these problems, each associated with a particular political ideology

1. Free market approach
- **Problem:** market inefficiencies, lack of entrepreneurial culture and excessive state intervention.

2. Direct state intervention (Spatial Keynesianism)
- **Problem**: structural weakness, fundamental deficiency in investment.

See Armstrong and Taylor 2000 pp 209 - 213

What have been the main phases of regional policy since 1928?
- **Industrial Transference**: facilitate the transfer of workers
- **Special areas Act**: taking "jobs to the workers".
- **Barlow Report**: commitment to full employment
- **Post war labour government**: loans and grants to firms, + controls on the location of industry.
- **Policy revival: (1958 – 1970):** Concern over post-war economic performance excessive growth in Greater London
- **Second revival (1972 – 79):** Policy revived but lack of mobile investment
- **Regional policy downgraded post 1979**: Abolition and reductions - rise of urban policy - Emergence of EC Regional Development Fund meant burden of expenditure could be switched. Focus sharpened, Encourage self-help, Switch from automatic to selective assistance (picking winners).

New participants:
The EU, Regional Development Agencies, Local Authorities and partners

Reading Armstrong and Taylor 2000 pp 214 - 225

Regional Policy and the manufacturing sector (See Harris, 1991, Chapter 1)
Until recently policy has been limited to helping manufacturing.
There are two main reasons:
- Manufacturing industries in various parts of the nation are generally in competition with each other.
- Manufacturing is more likely to embody attributes of self-sufficiency leading to "self-reliant" growth
  - not dependant on local demand alone
  - dominates other sectors through linkages
  - demand grows as national income grows
  - ability to innovate
  - ability to expand over time at an increasing rate

Economic efficiency or social inclusion?
There are two problems with regional policy
1) It has been set multiple objectives and
2) There might be a tension between social and economic objectives.

In its first guise policy may have been viewed as two objectives that were mutually compatible - reducing poverty in poor areas (social); and increasing labour supply in areas that had shortages (efficiency)

The Barlow Report had 3 objectives.
1. Reduce chronic unemployment in certain heavily depressed areas
2. Achieve a better balance in the geographical distribution of industry in order to alleviate congestion and over crowding in London
3. Achieve a better dispersion of industry for defensive and strategic purposes

Two reasons for the switch to social inclusion in the early to mid 90s
Growing inequality in income distribution
Growth of multiple deprivation - certain groups find it hard to escape from the poverty trap.

Arguments against using regional policy for social inclusion
1. The definition of social exclusion is vague and includes non-economic variables.
2. Social exclusion is a national problem and it requires a national solution and national policy to achieve that end.
3. Policies to deal with social exclusion are in conflict with those seeking to improve competitiveness.

Despite the arguments social inclusion is now firmly part of the regional economic agenda - in part this is because specific EU initiatives have an explicit social element particularly those that form part of the Community Economic Development Programme.

Conclusion

Armstrong and Taylor and strongly suggest that regional policy has suffered over the years from the lack of precise specification of its objectives. If objectives are not clear then evaluation becomes an exercise in measuring the **effects** rather than the **effectiveness** of regional policy.
They argue for objectives to be set in quantitative terms:

- Numerical targets against each objective (number of jobs created)
- Time period in which the objective is to be achieved (over next three years)
- Weight to be attached to each objective so that priorities can be determined

Armstrong and Taylor and Temple have suggested that the main reason why objectives were not specified clearly in the past is the fear of politicians that targets might not be achieved. In addition, it is sometimes difficult to measure exactly how many new jobs are as the result of policy and how many might have been created anyway without any intervention.

Things have changed since the early 90s - the setting of targets and indicators has become widespread both in the EU and the UK. However, A & T warn that policy drift is setting in with multiple, potentially conflicting objectives being set for a policy agenda, which is under-funded. They suggest that while there are plenty of targets there are too many policy instruments to achieve any of then effectively. This is not just a side-swipe at the inclusion of social objectives but a warning that there is a lack of focus and too much fragmented effort to make real progress in reducing regional disparities.

Further Reading

Armstrong & Taylor, (2000) Regional Economics & Policy, Blackwell, Oxford, Chapter 6, pp 143 – 153 & Chapter 7, pp 184 - 199 and Chapter 8, pp 205 – 231

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